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January 15, 2002

BY E-MAIL

PUBLIC VERSION

Ms. Gloria Blue
Executive Secretary
Trade Policy Staff Committee
Office of the U.S. Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508

Re: Rebuttal Comments On Potential Presidential Action Under Section 203 Of The Trade Act Of 1974 With Regard To Imports Of Semi-finished Carbon And Alloy Steel Slab

Dear Ms. Blue:

On behalf of the AK Steel Corporation, California Steel Industries, Inc., Duferco Farrell Corporation, and Oregon Steel Mills, Inc., we submit these rebuttal comments on potential Presidential action under Section 203 of the Trade Act of 1974 with regard to imports of semi-finished carbon and alloy steel slab. This document has been filed in Adobe PDF format via e-mail by the deadline of January 15, 2002, in accordance with the instructions in the Federal Register notice of the Trade Policy Staff Committee: Public Comments On Potential Action Under Section 203 Of The Trade Act Of 1974 With Regard To Imports Of Certain Steel (66 Fed. Reg. 54321, Oct. 26, 2001), as modified by the Federal Register notices published on November 29, 2001 (66 Fed. Reg. 59599) and December 28, 2001 (66 Fed. Reg. 67349).

We have removed information in brackets on page 17 and in Exhibit F of the attached public version. In the filing of the business confidential version, we requested that this information be accorded business confidential treatment and be exempted from public inspection, in accordance with 15 C.F.R. § 2003.6. This information relates to trade secrets and/or commercial and financial information, the disclosure of which is not authorized by the interested parties furnishing the information and is not required by law. The information for which we request business confidential treatment cannot be further summarized, aggregated, ranged, or indexed.

If you have any questions regarding this submission, please contact the undersigned.

Respectfully submitted,

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BEFORE THE
UNITED STATES TRADE REPRESENTATIVE

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<u>PUBLIC VERSION</u>
Business confidential information has been deleted from page 17 and Exhibit F.

REBUTTAL COMMENTS ON POTENTIAL PRESIDENTIAL ACTION ON SEMI-FINISHED STEEL SLAB

On Behalf Of

AK Steel Corporation, California Steel Industries, Inc., Duferco Farrell Corporation, And Oregon Steel Mills, Inc.

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January 15, 2002

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I. EXECUTIVE SUMMARY

In recommending a tariff-rate quota ("TRQ") rather than a straight tariff on slab, the U.S. International Trade Commission ("ITC") made the following findings:[1]

- Historically, commercial sales of domestically produced slab have been extremely limited
- Domestic producers typically consume nearly all the slab they produce to make higher-value downstream products
- While some slab sales do take place, the overall supply is inadequate to satisfy the needs of slab purchasers on a long-term basis
- The domestic producers that are particularly dependent on slab purchases include those that have no slab-making capability and those that have significantly more rolling capacity than slab-making capacity
- Some of these producers have recently restructured by closing down obsolete slab-making capacity and/or have made long-term investments in capacity to produce plate and sheet
- Integrated producers also require purchased slabs during furnace re-lines or other melt shop outages
- Imposition of a tariff on plate and sheet will itself generate increased adjustment-related need for slab imports in the short run due to (1) higher production of plate and sheet; (2) producers temporarily reducing slab-making capacity in order to shift to more modern slab-making equipment; and (3) producers upgrading or repairing existing equipment.

Vice Chairman Okun made additional findings:

- Most domestic integrated producers have exhibited sporadic willingness to sell slab to their domestic competitors
- Minimills have never sold slab to the open market

[1] Exhibit A to these comments contains the ITC's full explanation for its TRQ recommendation on slab.

- Geneva Steel, one of the few domestic producers that showed any consistent desire to market slabs, has temporarily shut down its hot end

- Even when Geneva was in operation, domestic merchant market sales of slab were less than one percent of total U.S. slab shipments

- Certain domestic producers of plate and sheet have business models that require the purchase of slab.

Based on these findings, the ITC recommended a TRQ, rather than a straight tariff, on slab in order "to avoid causing harm to domestic steel producers that have legitimate needs to continue to import slabs. . . ." ITC Report at 365. As Vice Chairman Okun added, a tariff remedy on slab "would have a potentially severe impact on the members of the domestic industry that need a reliable source of slab." Id. at 456.

In their January 4 comments to the TPSC, petitioners have submitted no evidence or argument that was not considered by the ITC or that would cast any doubt on the ITC's findings that a straight tariff on slab would harm members of the domestic industry that the import relief is supposed to benefit.

The ITC stated that its proposed 7 million ton TRQ would not be triggered under recent market conditions. Based on new information provided to the TPSC in our January 4 comments, however, domestic producers' legitimate needs for non-Canadian slab imports may exceed the proposed TRQ level by over 3 million tons. Thus, the President should impose no import restrictions on slab in order to avoid harming members of the domestic industry that depend on slab imports. Alternatively, the President should modify the proposed TRQ by increasing the quota level, reducing the above-quota tariff, and shortening the TRQ's duration.

II. PETITIONERS' SLAB ARGUMENTS ARE SERIOUSLY FLAWED

A. Slab And Flat-rolled Products Are Not Closely Related In Processing And Do Not Compete With Each Other

Petitioners assert that "flat products are closely related in processing and have dependent market relationships" and that "slab imports more broadly compete with the domestic producer shipments of hot-rolled and other downstream products." Schagrin at 13. Both statements are false.

First, slab and flat-rolled products are made in separate facilities using distinct production equipment, processes, technology, and employees. Slab is cast from liquid steel in the raw steelmaking process -- the hot end. Plate and sheet are rolled from slab in the rolling and finishing end. Slab cannot be made in a rolling mill; plate and sheet cannot be made in a slab-casting facility. Rolling changes the metallurgy of the steel. Slab is brittle and cannot be stamped, drawn, or bent; plate and sheet are strong and malleable and thus can be formed into end-use products.

Second, slab imports do not compete with domestic plate and sheet. The metallurgy, shape, weight, and size of slab make it totally unsuitable for end use. "Since slab is the core product from which carbon and alloy flat products are produced, there are no substitutes for this form of steel." ITC Report at FLAT-53. In fact, Dewey/Skadden admitted that slab is not "like" plate and sheet and that slab is not a substitute for plate and sheet.[2] Moreover, unlike plate and sheet, only steel mills buy slab.

[2] See Dewey/Skadden's September 28, 2001 Post-hearing Brief On Injury, Exh. A at 8, 11, 18.

B. Imports Do Not Give Slab-purchasing Mills A Cost Advantage

Contrary to petitioners (Dewey/Skadden at 17; Steelworkers at 4), slab imports do not give slab-purchasing mills a cost advantage over mills that produce their own slab.

Our post-hearing ITC brief on remedy set forth compelling evidence that the pricing of slab imports has conferred no advantage on slab-purchasing mills. First, we showed that monthly import prices for slab move in tandem with those for steel scrap and pig iron. See attached Exhibit B. Each of these raw materials was at the bottom of the pricing cycle during 2001, because their prices are largely determined by demand and prices for plate and sheet, which were depressed during 2001. Second, we demonstrated that AK Steel, California Steel, Duferco Farrell, and Oregon Steel do not undersell their slab-producing competitors in domestic flat-rolled markets. The evidence, most of which is confidential and subject to the ITC's Administrative Protective Order, compared the average unit values for the seven specific products on which the ITC collected pricing data. The pricing of AK Steel, California Steel, Duferco Farrell, and Oregon Steel was compared in each of the 22 quarters to the industry-wide domestic average, as reported in the ITC's Staff Report. For every product where pricing data was available, the comparisons showed that the four companies were tightly bunched around the trend for the entire domestic industry. See Slab Purchasers' November 13, 2001 Post-hearing Remedy Brief On Slabs, at 20.

In sum, slab imports do not provide a cost advantage to slab purchasers. Slab prices -- like those for steel scrap, pig iron, and other raw materials used to make plate and sheet -- rise when demand and pricing are strong for plate and sheet and fall when demand and pricing are weak for plate and sheet. Thus, the cost of imported slab is sometimes more and sometimes less than the cost to produce slab in the United States.

C. Restrictions On Slab Imports Are Not Needed To Fill The Hot End

The claim made by the Minimill 201 Coalition that domestic hot ends will not "fill" without "meaningful" restrictions on slab imports is false. See Schagrin at 30. First, excess slab capacity is not dragging down the fortunes of the flat products industry. Although the ITC found a "significant idling of the domestic industry's productive facilities," capacity utilization for slab was higher than for plate and sheet during the entire period of investigation ("POI"). See ITC Report at 52. Moreover, from 1996 to 2000, slab production increased by 5.3 percent,[3] and capacity utilization fell only because capacity increased even more, by 12.2 percent. Id. at Table FLAT-C-2. In fact, domestic slab capacity grew every year of the POI, regardless of whether the much smaller quantity of slab imports grew or declined.

Second, unused slab capacity is not due to slab imports, it is due to depressed demand for domestic plate and sheet. Thus, the way to fill up the hot end is to place import restrictions on plate and sheet, which will increase demand for domestic plate and sheet. Import restrictions on plate and sheet would create more demand for captively consumed slabs to supply domestic plate and sheet mills. This would increase slab capacity utilization and decrease unit fixed costs of slab production.

[3] In contrast, in the 1984 Section 201 case on steel, slab production plunged 38.4 percent from 1979 to 1983. Carbon and Certain Alloy Steel Products, Inv. No. TA-201-51, USITC Pub. 1553 at 19 (July 1984) {hereinafter 1984 Steel 201 Case}.

Commercial slab sales account for only 0.5 percent of the net sales value of the domestic industry's commercial shipments, and commercial sales of plate and sheet account for the remaining 99.5 percent.[4] Id. at FLAT-24-28. As a result, the imposition of import restrictions on plate and sheet, not slab, will improve the financial performance of the entire flat products industry, including slab production. Restrictions on slab would increase raw material costs and hurt the financial performance of domestic producers like AK Steel, California Steel, Duferco Farrell, and Oregon Steel that depend on foreign slab. Because restrictions on plate and sheet will increase slab capacity utilization, restrictions on slab imports would go beyond the remedy needed to redress serious injury to the domestic industry.

D. Unrestricted Slab Imports Would Not Force U.S. Producers To Close Their Hot Ends

Equally false is petitioners' claim that without restrictions on slab imports, domestic slab producers will be forced to close their hot ends. See Schagrin at 31; Dewey/Skadden at 17.

First, there is not a single piece of evidence that a domestic producer of slab has ever closed its hot end because of slab imports.[5] In fact, despite there being no import restrictions on slab during 1996-2000, slab capacity increased 12.2 percent during this

[4] Annual revenue during 1996-June 2001 averaged $132,075,000 for slab and $26,974,395,000 for the flat products industry (slab, plate, hot roll, cold roll, and coated).

[5] Counsel for petitioners claimed during the ITC hearings that slab imports caused "three major slab production facilities" to shut down: LTV Cleveland West, Gulf States, and Trico. Injury Tr. at 482. In our September 28, 2001 posthearing brief on injury before the ITC (page 50), we demonstrated that this claim was bogus. No producer cited slab imports as the cause of a closure during the POI, and

period. See ITC Report at Table FLAT-C-2. Second, no evidence exists that a domestic slab producer is planning to close its hot end as the result of slab imports. In fact, Bethlehem Steel, LTV Steel, National Steel, and United States Steel admitted that "{a}s of now, none of Domestic Producers has any specific plans to reduce capacity beyond what has recently been announced publicly." See Dewey/Skadden November 13, 2001 Posthearing Remedy Brief, at E-1.

Third, no integrated producer could afford to shutter enormous hot end fixed assets in order to replace their slab production with slab imports. Fourth, contracting out and employment security clauses in collective bargaining agreements prevent integrated producers from shutting down their hot ends. See Slab Purchasers' November 13, 2001 Post-hearing Remedy Brief On Slabs, at 35. Fifth, the environmental costs of shutting down a hot end are enormous. See Remedy Tr. at 398.

Sixth, a slab importing model is risky. Slab prices go up and down. At the peak of the steel demand cycle, the price of imported slab generally exceeds the cost to produce slab in the United States. The representative of AK Steel testified before the ITC, for example, that his company "{m}any times . . . purchases slabs that are in excess of our costs to manufacture those same slabs. . . . {W}e paid more for slabs in the year 2000 than it costs us to make them domestically." Injury Tr. at 586-87. Finally, there is no assurance that sufficient merchant slab will be available at the peak of the demand cycle, when foreign producers would rather convert their own slab into higher value-

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merchant slab sales were not a significant part of any operations that shut down. For a discussion of Geneva Steel's closure, see Section II.I, infra.

added plate and sheet. As testified by the representative of AK Steel, "I don't know of anyone who is intending to completely de-integrate … and put themselves at total risk of trying to buy all slabs and only have rolling facilities." Id. at 612.

Thus, no evidence supports petitioners' shrill rhetoric that the domestic industry's hot end will somehow be "hollowed out" by a flood of imported slabs. On the other hand, import restrictions on slab will hollow out U.S. rolling mills dependent on foreign slab. Mills with no hot end like California Steel, Duferco Farrell, and Lone Star cannot survive without slab imports. Import restrictions on slab would also jeopardize the successful business models of companies like AK Steel and Oregon Steel. These companies produce most of their own slab, but need imported slab to supply their state-of-the-art rolling mills, that were predicated on their access to foreign slabs.

E. A Substantial Portion Of The Benefits Of A Tariff Remedy Would Not Be Lost If The Tariff Were Not Applied To Slab

Dewey/Skadden argue at 18 that meaningful relief is not possible with the ITC's proposed TRQ on slab. In footnote 48, they claim that removing slab from their 40 percent remedy proposal would reduce the revenue effect by ten percent and the income effect by 38 percent.   According to their Exhibit 1, use of a TRQ on slab instead of a 20 percent tariff on all flat products would reduce the revenue effect by 6 percent and the income effect by 31 percent. These claims of reduced revenue effects and grossly exaggerated income effects are all based on the flawed and self-serving CRA economic model, which the ITC did not accept for good reasons.[6] The ITC's own linked, multi-market model also shows that removing slab from a 20 percent tariff on all flat products would have reduced revenue effects, but those effects are exaggerated due primarily to implausible inputs for the elasticities of substitution and domestic supply.[7] As concluded by Vice Chairman Okun, "less weight {should be given} to the models for slab as they do not take into account the inconsistent availability of supply of slabs from domestic sources." ITC Report at 456.

Moreover, Dewey/Skadden ignore the fact that the exaggerated benefits they claim their clients would receive from tariffs on slab would come at the expense of other members of the same domestic flat products industry that purchase slab. That is, tariffs on slab would shift revenue and income away from some members of the industry to other members of the same domestic industry. As noted by Vice Chairman Okun, "{c}ertain domestic producers of certain flat-rolled steel have business models that require the purchase of slab, and thus the importation of slab to ensure a steady, dependable supply of their feedstock." Id. It would be unfair to shift income and revenue away from those producers, as proposed by Dewey/Skadden, especially since "{s}ome of those domestic producers have recently restructured by closing obsolete

[6] See LECG Economic Analysis Of Remedy Model Submissions, Exhibit M to Slab Purchasers' November 13, 2001 Post-hearing Remedy Brief On Slabs.

[7] The elasticity of substitution should be very low for slab, because over 99 percent of domestic slab is captively consumed and does not compete with imported slab. The elasticity of domestic supply for slab is very low because domestic slab producers generally do not sell slab into the merchant market.

capacity and made, or are making, long-term investments that depend on purchases, and thus imports, of slab." Id.

F. The Benefits Of A Tariff On Plate And Sheet Would Not Offset Increases In Raw Material Costs From A Tariff On Slab

Contrary to the repeated assertions of petitioners (see, e.g., Dewey/Skadden at 21), the benefits of a tariff on plate and sheet products would not offset increases in raw material costs from a tariff on slab. Because the U.S. has enormous unused capacity for plate and sheet, a tariff on plate and sheet imports is not likely to have any significant short-term impact on domestic prices. Instead, purchases will shift away from imports toward domestic sources. This will enhance domestic mills' market share and revenue, but not their prices.

A tariff on slab would instantly convert efficient slab-consuming steel producers into high-cost suppliers in a market where higher costs cannot be passed on to consumers. Each dollar paid for a tariff would increase raw material costs by a dollar and decrease profits by a dollar. Some slab purchasers might be forced into bankruptcy and/or forced into prematurely selling their assets at bargain basement prices to a financially sound domestic competitor like Nucor. Others, like AK Steel and Oregon Steel, which are only partially dependent on slab imports, would have their entire business model undermined and suffer losses in profitability. The significance would be magnified because recent major capital investments (AK Steel's Rockport Works and Oregon Steel's Portland Plate Mill) were predicated on access to slab imports.

G. Slab Purchasers Could Not Avoid Tariffs On Slab By Switching To Domestic Slab

Petitioners argue that a tariff on slab would not hurt domestic slab purchasers because they could avoid tariffs by purchasing domestic slab. See, e.g., Dewey/Skadden at 22; Schagrin at 29. This argument assumes that domestic slab is available for purchase on the merchant market. To the contrary, all evidence demonstrates that domestic slab is not, and has never been, consistently available for purchase on the merchant market.

First, domestic slab for the merchant market has been virtually non-existent for at least two decades:

- In the 1984 Steel 201 Case, the ITC stated that "{s}emifinished products are normally captively consumed within the producers' facility for processing into more advanced products."[8]

- In 1994, the ITC noted that "{s}everal companies have stated that they sold surplus semifinished products on the open market, but few do so regularly. Instead, most try to enter the market when steel demand is low (and the market for their finished steel output has diminished) and exit the market when steel demand is high (and the company would rather roll all the steel it can melt)."[9]

- In the current Section 201 case, the ITC found that "historically, commercial sales of domestically produced slab have been extremely limited. Domestic producers typically internally consume nearly all the slabs they produce to make higher-value downstream products. While some slab sales do take place, the overall supply is inadequate to satisfy the needs of slab purchasers on a long-term basis." ITC Report at 365. "{M}ost domestic integrated steel producers have exhibited sporadic willingness to sell to their domestic competitors, and minimills have never sold slab on the open market." Id. at 456.

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[8] 1984 Steel 201 Case, at 19.

[9] U.S. Int'l Trade Comm'n, Pub. 2758, Industry and Trade Summary: Semifinished Steel 5 (Mar. 1994).

- Commerce recently found in its Section 232 investigation that "very little semi-finished steel is available on the U.S. merchant market."[10]

Thus, domestic producers have never consistently sold slab on the merchant market, even when slab prices were substantially higher than today.

Second, over 99 percent of domestically-produced slab is internally consumed by steel producers to make flat-rolled products. Id. at FLAT-1. Thus, slab purchasers have no choice but to turn to imports to satisfy their legitimate needs for slab. While petitioners claim that they would sell more slab on the merchant market if slab prices were higher (see, e.g., Dewey/Skadden at 22), there are 14 million tons more rolling capacity in the U.S. than slab-making capacity. Consequently, even integrated producers must purchase slab to fully utilize finishing capacity and during furnace re-lines and other melt shop outages.

Third, no economic incentive exists for domestic mills to sell slab to their competitors as a raw material in the production of plate and sheet in competition with their own products. Even at the peak of the demand cycle, when slab prices are highest, integrated producers do not want to sell slab, because they would rather sell plate and sheet, which also have their highest prices at the top of the demand cycle.

[10] The Effect Of Imports Of Iron Ore And Semi-finished Steel On The National Security, U.S. DOC, Export Administration, October 2001, at 11.

H. Flat-rolled Prices Can Significantly Improve Without Restrictions On Slab Imports

Petitioners maintain that flat-rolled prices cannot improve without restrictions on slab imports. See Schagrin at 26. The argument rests on the mistaken belief that slab imports are capable of lowering the entire price structure of domestic plate and sheet.

First, slab imports are too insignificant to affect domestic prices for plate and sheet. Slab imports account for only 9.7 percent of domestic slab consumption, ITC Table FLAT-C-2, and "virtually all U.S.-produced slab is internally consumed by the domestic slab producers in their production of hot-rolled steel (sheet, strip, or plate)." Id. at FLAT-39. Slab imports account for only 0.5 percent of the net sales value of the domestic flat products industry. Id. at FLAT-24-28.

Second, we retained LECG to determine whether there was any indication that the prices of slab imports were determining the prices of domestic plate and sheet. LECG performed Granger causality tests, which clearly establish the direction of price influence as flowing from the price of the finished product back to slab, not the reverse. See Slab Purchasers' September 10, 2001 Pre-hearing Injury Brief on Slab, at Economic Appendix D. This economic evidence was corroborated with ITC hearing testimony.[11] The ITC agreed. It found that downstream prices for hot roll and cold roll influence the price of slab, but not vice versa. ITC Report at 43.

These facts refute any claim that flat-rolled prices cannot improve without import restrictions on slab. Slab import prices are simply incapable of influencing the entire

[11] Injury Tr. at 559 (Mr. Gonçalves); Id. at 589 (Mr. Gonçalves); Id. at 591 (Mr. Corvin).

price structure of domestic plate and sheet. Indeed, for as long as one can remember, the prices of plate and sheet have risen in response to favorable supply and demand conditions -- notwithstanding the fact that slab imports have not been restricted.

I. Geneva Steel Did Not Shut Down Due To Slab Imports

Petitioners' claims that Geneva Steel's shutdown was a result of slab imports (Schagrin at 10) are contradicted by Geneva's own statements to Commerce, a federal bankruptcy court, and the Securities and Exchange Commission.

Geneva has readily admitted that imports of downstream finished steel products are the primary source of the company's financial troubles. In an April 6, 2001 letter to Commerce attached to our ITC pre-hearing injury brief (Exhibit 40), Geneva stated that "the flood of finished steel products forced the Company into Chapter 11 bankruptcy protection in March 1999" and that "unfair imports of finished steel products have been the primary cause of the sales declines experienced by Geneva. . . ." (emphasis added). In its bankruptcy "Disclosure Statement" filed with the U. S. Bankruptcy Court for the District of Utah (Central Division), Geneva refers to injury from various flat and tubular products, but not once does it refer to injury from slab imports. Also, Geneva has never cited any injury from slab imports in its SEC filings.

Slab imports did not force Geneva to shut down its furnaces, because Geneva has never been in business primarily to sell slab, and slab has never constituted a major product line. As demonstrated in our ITC post-hearing injury brief (64-66) and affidavits attached to that brief from Mr. Wright of California Steel and Mr. Rowan of Oregon Steel (Exhibits C & E), Geneva has never been a consistent and reliable supplier of slab; it cannot produce and, in fact, is unwilling to produce many of the slab specifications most needed by those two mills. As Mr. Wright testified, "California Steel has experienced situations in which Geneva put delivery of finished products to other customers ahead of slab deliveries to us. Mr. Johnsen has stated often that it is Geneva's intention to be a major player in the plate and coil markets." (Aff. of Vicente Wright at ¶15). Finally, Geneva's claims to the ITC that it was willing and able to sell large quantities of slab were flatly contradicted by (1) documentary evidence of its sporadic offers of negligible slab quantities and its preference to sell plate and sheet and (2) the announcement of the closing of its plant one day after it made such claims to the ITC. See Slab Purchasers' September 28, 2001 Post-hearing Injury Brief On Slab, at Exhibits C (Wright Aff.) and E (Rowan Aff.).

J. Slab Imports Do Not Sustain Excess, Inefficient Foreign Capacity

Petitioners' claim that slab imports permit excess, inefficient foreign capacity to remain in production is also wrong. See Dewey/Skadden at 17.

First, all of the increase in slab imports during 1996-2000 is attributable to the $1.5 billion invested in new rolling capacity by AK Steel, California Steel, Duferco Farrell, and Oregon Steel. See Slab Purchasers' January 4, 2002 Submission To TPSC, at Exhibit 9. Absent their investments during 1997-1999, U.S. slab imports would have declined by over half a million tons. Most of the slab imported by these companies comes from just three countries: Brazil, Mexico, and Australia. The slab producers in these countries operate some of the most modern and efficient facilities in the world.

Second, any excess and inefficient slab capacity does not exist because of slab exports -- it exists because foreign governments have been supporting their steel companies with subsidies and other assistance for over a quarter century. Imposing restrictions on U.S. slab imports would not address this problem. Government intervention and its legacy of excess, inefficient global capacity can only be addressed by meaningful disciplines on government intervention in the market.

III. RESPONSES TO QUESTIONS FROM THE TPSC

A. New Information That Was Not Provided To The ITC

1. The TRQ recommended by the ITC will harm domestic steel producers that are dependent on slab imports

The ITC recommended a TRQ instead of a tariff on slab in order to "avoid causing harm to domestic steel producers that have legitimate needs to continue to import slabs . . . ." ITC Report at 365. Information provided to the TPSC (but not to the ITC), however, demonstrates that the proposed remedy will not avoid causing harm to domestic producers dependent on slab imports.

First, the 7 million ton quota recommended by the ITC is based upon the level of non-Canadian slab imports in the year 2000. Id. While the ITC stated that the depressed demand conditions in the first half of 2001 suggest that the quota level likely "would not be triggered" in the first year of import relief, information not previously considered by the ITC demonstrates this is not the case.

Demand for foreign slab in the first year of relief is likely to be at least 3 million tons greater than in 2000. As shown in our January 4 submission (Exhibit 10), the following quantities of additional slab will be needed: (1) 200,000 tons to replace domestic slab production lost from Geneva Steel's closure on November 14, 2001; (2) 800,000 tons as a result of CSN's acquisition of Heartland's rolling mill; (3) 975,000 tons to supply the increased demand for domestic plate and sheet as a result of import restrictions on those products; (4) 700,000 tons to replace lost domestic melt capacity as a result of additional furnace relines; and (5) 800,000 tons needed by Wheeling-Pittsburgh to carry-out its adjustment plan. While these requirements alone total over 3 million additional tons, substantial tons also may be needed to replace domestic slab production lost as a result of industry consolidation/rationalization and increased environmental controls on coke ovens and blast furnaces.

Second, AK Steel, California Steel, Duferco Farrell, and Oregon Steel will require at least [ ] more tons of foreign slab in 2002 than they did in 2000 to meet projected demand for their plate and sheet products, as indicated in our January 4 submission to the TPSC (Exhibits 2-5).

Third, when determining that a 20 percent tariff on over quota imports would "avoid causing harm to domestic steel producers," the ITC did not consider the impact of the TRQ on the bidding process for slab purchases. As explained in Exhibits C-F, because the proposed TRQ would impose a sharp 20 percent input cost penalty on late orders beyond the TRQ threshold, it would force slab purchasers to reduce their risk exposure by moving forward their orders for slab. Given the first-come, first serve nature of any TRQ, this would bid the price of slab imports up far in advance of the TRQ starting to bind. Foreign slab suppliers would be able to exploit this situation by approaching their traditional slab customers early in the year and insisting upon large orders at premium prices in order for their customers to avoid the risk of paying a 20 percent tariff on above-quota imports at the end of the year. Thus, the TRQ would have a substantial impact on prices even if foreign slab demand did not reach 7 million tons.

2. Slab imports do not threaten national security

In its recent Section 232 investigation, Commerce concluded that imports of semi-finished steel do not threaten national security because, among other things, the U.S. steel industry produces three times the maximum amount of semi-finished steel that might be required for national security purposes. Commerce made several other findings that confirm that slab imports do not injure domestic producers and, therefore, import restrictions on slab are not necessary. The ITC did not have the benefit of this report when it recommended a TRQ on slab imports. Specifically:

- Semi-finished steel imports account for only 7 percent of total U.S. consumption of semi-finished steel or, as characterized by Commerce, "a modest proportion of total U.S. consumption." Final 232 Report, at 2.

- While "domestic production of . . . semi-finished steel far exceeds the amounts necessary to satisfy U.S. national security requirements . . . , {o}f the semi-finished steel that is produced in the United States, most is consumed within the integrated or mini-mill producer's facility for processing into finished steel products. As a result, very little semi-finished steel is available on the U.S. merchant market." Id. at 11, 18.

- Slab imports cannot be pushed into the U.S. market by foreign producers and will not "surge" as a result of import restrictions on plate and sheet. Rather, the level of slab imports will be determined by the demand for domestically-produced plate and sheet: "Growth in . . . semi-finished steel production is principally driven by downstream demand. Semi-finished steel production is sensitive to consumer demand for finished steel products, particularly demand for automobiles, construction, machinery, and appliances." Id. at 26.

- Semi-finished steel imports benefit the domestic steel industry. According to Commerce, "the U.S. steel industry utilizes semi-finished steel imports to supplement its own production." In addition, "U.S. steel mills also use imported semi-finished steel to continue finished steel production when their blast furnaces or basic oxygen furnaces are down for repairs or maintenance (e.g., relining). Further, some producers, including mini-mills, import high-quality semi-finished steel in order to produce high quality, specialty steels that they could not otherwise make." Id. at 31 & n.47.

- Semi-finished steel imports have not hollowed out the hot end of the steel industry. In fact, U.S. semi-finished steel production capacity increased over 10 percent from 1999 to 2000. Id. at 22.

B. There Were No Blast Furnace Relines In 2001

According to Metal Strategies, no furnaces were relined in 2001. This fact partly explains why slab imports were lower in 2001 than in 2000. In 2000, one blast furnace with 1 million tons of annual capacity was relined. In contrast, 12 blast furnaces with 5.25 million tons of average annual capacity are expected to be relined in 2002-2005. The average annual capacity relined during 2002-2005, therefore, should exceed that relined during 2000 by at least 4.25 million tons. The ITC's proposed quota level does not take into account the additional 700,000 tons[12] of slab that will be needed while this capacity is shutdown for reline.

C. The Economic Models All Demonstrate That Higher Slab Costs Would Not Be Offset By Higher Prices For Plate And Sheet

Every single economic model run by petitioners and the ITC demonstrates that the higher slab costs incurred by slab purchasers as a result of a 20 percent tariff on slab

[12] As shown in our January 4 (Exhibit 10) submission, the average furnace reline requires 60 days of furnace downtime. To derive the 699,000 ton figure, we multiplied the 4.25 million tons of additional average annual capacity that will be relined during 2002-2005 by 60/365 (i.e., 60/365 x 4,250,000 = 699,000 tons).

would not be offset by higher prices for their sales of domestic plate and sheet as a result of a 20 percent tariff on plate and sheet. For example, Exhibit 1 to Dewey/Skadden's January 4 comments claims that a 20 percent tariff would increase the cost of imported slab by 15.29 percent, but increase the price of domestic plate and sheet by only 3.97 percent. The ITC's traditional, non-linked separate market model shows that a 20 percent tariff would cause slab import prices to jump 16.5 to 17.8 percent and domestic prices to increase only 0.4 to 1.2 percent for plate, 1.1 to 3.1 percent for hot roll, 0.7 to 2.5 percent for cold roll, and 0.3 to 1.0 for coated. Remedy Memorandum EC-Y-048 at Tables FLAT-6-10. The ITC's linked, multi-market model shows that a 20 percent tariff would cause slab import prices to jump 11.6 to 15.4 percent and plate and sheet prices to increase only 1.1 to 2.2 percent. Remedy Memorandum EC-Y-050 at Table 2.

The reason is easily explained. Domestic plate and sheet and imported plate and sheet are highly substitutable, ample excess capacity exists for domestic plate and sheet, and domestic producers are highly motivated to sell more plate and sheet into the merchant market. Thus, if a 20 percent tariff were imposed on imported plate and sheet, consumers would readily shift their purchases away from foreign plate and sheet toward domestic plate and sheet, with little or no change in the market price. In economic terms, domestic plate and sheet and imported plate and sheet have a very high elasticity of substitution, and domestic supply for plate and sheet also is highly elastic. In contrast, over 99 percent of domestic slab is captively consumed, domestic rolling capacity exceeds slab capacity by 14 million tons, domestic slab producers have no economic motivation to sell slab to their domestic competitors, mini-mills cannot sell slab, and domestic slab only rarely competes with imported slab in the merchant market. Thus, a 20 percent tariff on slab would not cause slab purchases to shift from imported to domestic slab. Instead, slab purchasers would have to pay more for imported slab and suffer higher raw material costs. In economic terms, domestic and imported slab have a very low elasticity of substitution, and domestic slab has a very low elasticity of supply.

The economic models presented by petitioners and the ITC reflect this dichotomy, but grossly understate its degree. In economic terms, both petitioners and the ITC err by overstating the models' inputs for elasticity of substitution between domestic and imported slab and for the supply elasticity of domestic slab. The models assume, contrary to fact, that slab producers have the same or almost the same incentive and ability to sell slab into the merchant market as they have for plate and sheet.[13] But, as found by the ITC, "commercial sales of domestically produced slab have been extremely limited. Domestic producers typically internally consume all the slabs they produce to make higher-value downstream products." ITC Report at 365. As Vice Chairman Okun noted, "most integrated steel producers have exhibited sporadic willingness to sell slab to their domestic competitors, and minimills have never sold slab on the open market." Id. at 456. For this reason, the models for slab should be given less weight because they "do not take into account the inconsistent availability of supply of slabs from domestic sources." Id.

[13] For example, by inputting their models with a slab domestic supply elasticity of 2 to 4, Remedy Memorandum EY-Y-046 at FLAT-10, the ITC staff assume that a 5 percent increase in slab prices would cause domestic mills to increase their merchant slab sales by 10 to 20 percent. That assumption is simply ridiculous for slab.

Finally, it should be noted, as discussed more fully in Section II.H, above, that prices for merchant slab are largely determined by prices for hot roll. Id. at 43. Merchant slab prices do not dictate the prices of domestic plate and sheet. Thus, as the price of hot roll increases, the price of slab will likewise increase. This has always been the case and will continue to be the case, whether or not tariffs are imposed on slab. Accordingly, no way exists for slab purchasers to offset higher slab costs attributable to a tariff with higher prices on domestic plate and sheet.

IV. CONCLUSION

The President should not impose import restrictions on slab, because they are not needed to remedy the injury suffered by the domestic flat products industry, and because they would harm members of that industry. Alternatively, the President should modify the recommended TRQ by (1) increasing the quota level to at least 9 million tons in year one, 9.5 million tons in year two, and 10 million tons in year three; (2) reducing the additional tariff to no more than 10 percent in year one, 8 percent in year two, and 6 percent in year three; and (3) limiting the duration of the TRQ to three years and one day.

Joseph W. Dorn

Joseph W. Dorn
Duane W. Layton
Christine E. Savage

KING & SPALDING
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Dated: January 15, 2002

THE ITC'S RATIONALE FOR TRQ ON SLABS

Commission's Rationale (p. 365)

"In determining the appropriate import relief for slab, we considered the fact that, historically, commercial sales of domestically produced slab have been extremely limited. Domestic producers typically internally consume nearly all the slabs they produce to make higher-value downstream products. While some slab sales do take place, the overall supply is inadequate to satisfy the needs of slab purchasers on a long-term basis. The domestic producers that are particularly dependent on slab purchases include those that have no slab-making capability and those that have significantly more rolling capacity than slab-making capacity. Some of these producers have recently restructured by closing down obsolete slab-making capacity and/or have made long-term investments in capacity to produce further processed certain carbon flat-rolled steel. We note that integrated producers also require purchased slabs during furnace re-lines or other melt shop outages.

Our recommendation of a tariff-rate quota for imports of slab is intended to avoid causing harm to domestic steel producers that have legitimate needs to continue to import slabs, while at the same time providing some protection against additional surges in slab imports.

* * *

We are recommending an import level with no tariff for the first year of relief that is set at the level of imports of slab minus imports of slab from Canada in year 2000. While lower first-half 2001 imports of slab would suggest that this tariff-rate quota would not be triggered under recent market conditions, we expect that imposition of a tariff remedy on further processed carbon flat-rolled steel will itself generate increased adjustment-related need for slab imports in the short-term, due to such factors as higher production of further processed carbon flat-rolled steel, and producers temporarily reducing slab-making capacity in order to shift to more modern slab-making equipment, or to upgrade or repair existing equipment as part of their adjustment efforts. At the same time, our remedy avoids creating an additional incentive to increase slab imports."

Vice Chairman Okun's Rationale (pp. 456-457)

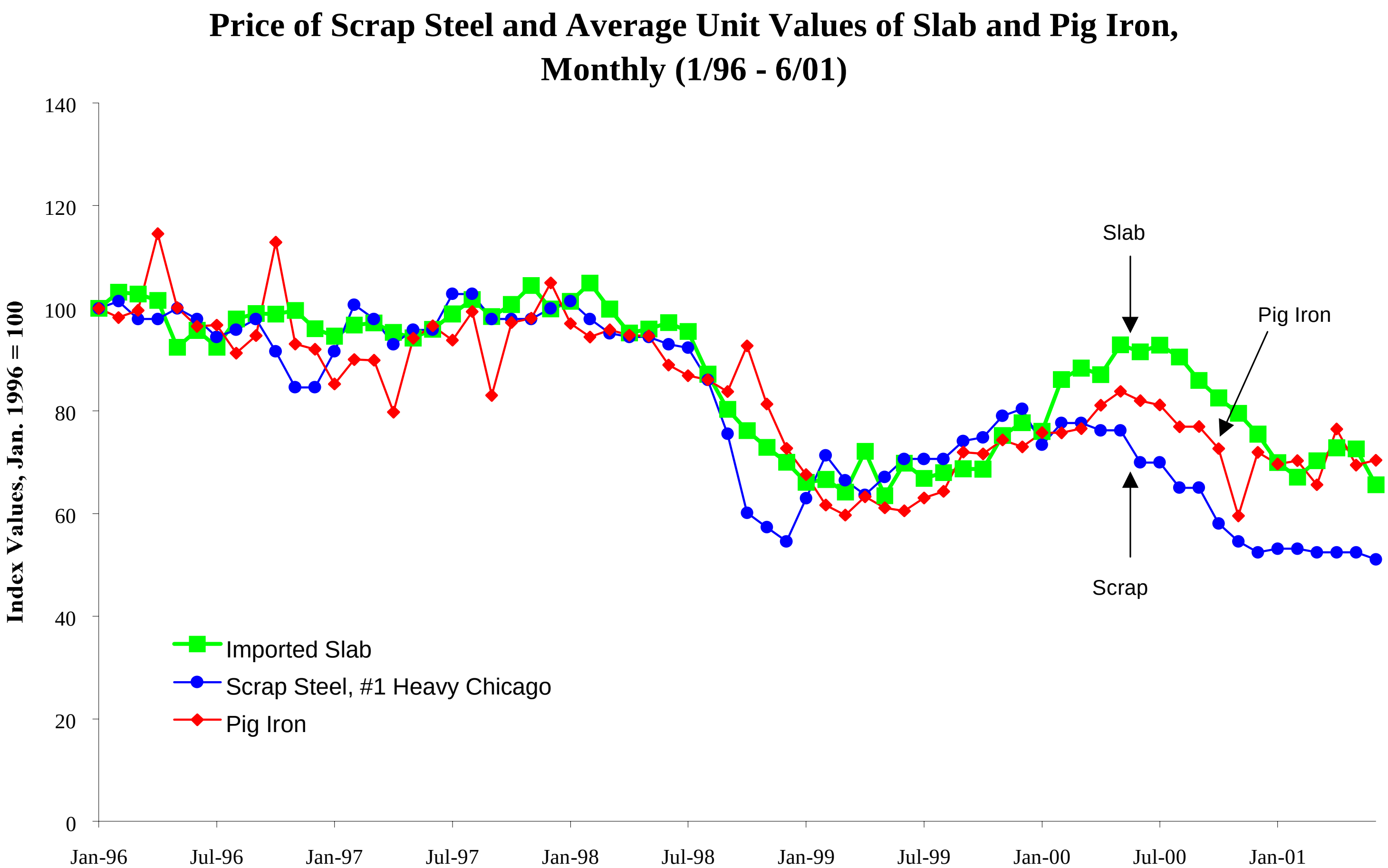
"In determining the appropriate import relief for slab, I considered the fact that historically, commercial sales of domestically produced slab have been extremely limited. Domestic producers typically internally consume nearly all the slabs they produce to make higher-value downstream products. While some domestic slab sales do take place, the record demonstrates that there is not a long-term supply of domestically-produced slab readily available. Testimony at the hearing and evidence provided in briefs indicates that most domestic integrated steel producers have exhibited sporadic willingness to sell slab to their domestic competitors, and minimills have never sold slab on the open market. This is particularly problematic given the fact that Geneva Steel, one of the few domestic producers that showed any consistent desire to market slabs, recently announced the temporary shut-down of its hot-end facilities. I note, however, that even when Geneva was in operation, domestic merchant market sales of slabs were less than one percent of total U.S. shipments.

I also considered the fact that the various economic models showed a great impact with certain quota levels and tariff levels on slab. However, I have given less weight to the models for slab as they do not take into account the inconsistent availability of supply of slabs from domestic sources.

Certain domestic producers of certain carbon flat-rolled steel have business models that require the purchase of slabs, and thus the importation of slab to ensure a steady, dependable supply of their feedstock. Some of these domestic producers have recently restructured by closing obsolete capacity and made, or are making, long-term investments that depend on purchases, and thus imports, of slab. Moreover, the evidence demonstrates that imports of slab are not only needed by processors of slab that have no hot-end capability, but also by producers that have more rolling capacity than slab producing capacity and integrated producers during furnace re-lines or other melt shop outages. Therefore, I recommend a tariff-rate quota for imports of slab that is intended not to harm domestic producers that have a legitimate need to continue to import slabs, including those that have made positive adjustments that depend on slab purchases. In doing so, I have considered the testimony of certain integrated producers at the remedy phase that the Commission recommend strong tariffs on slabs, and revisit the issue of supply concerns in any monitoring proceeding. However, I believe that to do so would have a potentially severe impact on the members of the domestic industry that need a reliable source of slab.

I note that there was testimony at the hearing in the injury phase of this investigation that members of the domestic industry were not against the use of slabs for those producers that used them to continue their operations, but rather were opposed to the flood that will occur in the future if some limits were not put on the importation of slabs. Indeed, there was concern expressed that the continued unfettered importation of slab would force other integrated producers to adopt a business model that relied on imported slab to support their rolling operations. A tariff-rate quota which permits the continued importation of slab at levels close to current imports will most alleviate the concerns expressed at the hearing and will not favor one domestic business model at the expense of another. I have recommended a tariff-rate quota rather than a quota because the tariff-rate quota will permit importation at current levels, but will also allow for additional importation under tariff should conditions develop that any domestic producer require additional slab feedstock to continue operations."

EXHIBIT A
(Page 2 of 2)



Sources: USITC Trade Dataweb for slab and pig iron; and *Purchasing Magazine* for scrap steel, #1 Heavy Chicago.

EXHIBIT B

PUBLIC VERSION

AK Steel Corporation
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Richard M. Wardrop, Jr.
CHAIRMAN AND
CHIEF EXECUTIVE OFFICER

January 14, 2002

The Honorable Robert Zoellick
United States Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508

Re: Section 201 – Investigation on Steel Imports

Dear Ambassador Zoellick:

AK Steel Corporation, a company whose steelmaking traditions trace back to 1900, is a $4.6 billion company with 11,600 employees and seven steelmaking and finishing plants in four states. AK Steel has developed a business plan that allows it to compete on a global scale, and for the last eight years, has led the steel industry in safety, quality, productivity and operating profit per ton.

The tariff-rate quota ("TRQ") on slabs recommended by the ITC, while not nearly as onerous as the tariff remedy advocated by some of our competitors, would unfairly injure AK Steel by driving up the cost of slabs, one of our basic raw materials. As explained below, under the ITC recommendation, our slab costs would increase even if demand for foreign slabs did not exceed the 7 million ton quota level recommended by the ITC.

The buying and selling of slabs is a steel mill to steel mill business. Unlike most products that have been the subject of Section 201 quotas or TRQs, slabs are not imported to be sold from inventory in the United States. They are imported by steel mills like AK Steel to fully maximize rolling capacity that would be under-utilized without available merchant slabs. Our foreign suppliers know that we and the other domestic mills must have slabs and that domestic mills will compete against each other to purchase the limited slabs that will be available. Foreign suppliers will use the threat of 20 percent tariffs on above-quota imports to force us to commit to large quantities of slabs at premium prices in order to ensure that we meet our slab needs with in-quota slabs. Our foreign suppliers know, as we do, that demand for foreign slabs is likely to exceed 7 million tons in the first year of relief. This likelihood will force slab purchasers to bid up the price for slabs early in the quota year whether or not demand in fact exceeds 7 million tons.

Imposing the recommended TRQ on slabs would put us at a competitive disadvantage to our domestic integrated steel mill competitors. These competitors do import some slabs when they must reline or repair equipment, or under other extraordinary circumstances, but not in large quantities as part of their business plan. Without the availability of foreign slabs, we would be at the mercy of our domestic competitors to purchase from them a fundamental raw material and, based on historical precedent, it is unlikely that they would sell to us on a consistent, reliable or commercially reasonable basis. Instead, they would convert their slabs to higher-margin finished product and use that finished product to take market share from us.

AK Steel Corporation

Further, the recommended TRQ on slabs would put us at a competitive disadvantage to our domestic minimill competitors who do not import slabs at all, but do import their key raw materials, such as pig iron, which are not subject to tariffs and quotas.

Because we have already rationalized and restructured our business (as the Bush Administration advocates is essential to the survival of our industry) without any request for tariffs or massive multi-billion dollar subsidies, it seems particularly inappropriate and inequitable to impose trade restrictions which would effectively penalize AK Steel for having already taken those difficult actions. That is precisely what will happen if the proposed TRQ is imposed on foreign slab imports. Furthermore, the domestic industry will be motivated to further ignore the need to rationalize, restructure and in turn revitalize its business.

Very truly yours,

Richard M Wardrop Jr

CALIFORNIA STEEL INDUSTRIES, INC.

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(909) 350-6200
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January 11, 2001

The Honorable Robert Zoellick
United States Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508

RE: Section 201 Investigation on Steel Imports

Dear Ambassador Zoellick:

On behalf of California Steel Industries, Inc., I am writing to explain how the tariff-rate quota ("TRQ") on semi-finished steel slab as recommended by the U.S. International Trade Commission would have adverse effects on slab prices. Specifically, a TRQ with an above-quota tariff of 20 percent would (1) bid up the price of slab imports in advance of the TRQ starting to bind and (2) make it cost prohibitive for California Steel to acquire slabs after the quota level is reached, forcing us to buy in advance.

Slab purchasing is a complex process. In CSI's case, we buy a significant tonnage of approximately 1.9 million tons of slabs on an annual basis. A foreign supplier's slab offer first must be evaluated to ensure that the supplier will provide a quality slab that meets our ISO 9000 standards. Our purchasing, metallurgical, and production control departments then must ascertain the technical abilities and production capabilities of the supplier to insure compatibility with our rolling schedules. Once these conditions are satisfied, our slab purchasing department begins negotiations with the supplier to determine tonnage, shipment timing, price, and other terms and conditions. Only after all of these steps are completed can an order be placed with the supplier.

We expect that foreign slab suppliers will use the TRQ to their advantage by approaching their traditional slab customers early in the year and insisting upon large orders at premium prices in order for their customers to avoid the risk of paying 20 % tariffs on above-quota imports at the end of the year. They would gain all of the leverage to negotiate terms, conditions, and prices to their satisfaction. They could effectively auction off their in-quota slab production at inflated prices. CSI could not risk saying "no," because we must have slab, and paying a 20 % tariff on above-quota slabs would eliminate any potential profit.

Because the proposed TRQ would impose a sharp 20 percent input cost penalty on late orders beyond the TRQ threshold, it would force slab purchases like California Steel to reduce their risk exposure by moving forward their orders for slab. Given the first-come, first serve nature of any TRQ, this would bid the price of slab imports up far in advance of the TRQ starting to bind. Thus, we would end up paying higher prices for slab even if foreign slab demand did not reach the 7 million ton quota level.

In addition, the recovery of the U.S. economy in 2002 will make CSI to buy more slabs in 2002 than we did in 2000. Accordingly, we also expect that total U.S. demand for foreign slab will far exceed 7 million tons in the first year of the proposed TRQ. Thus, we would be forced to pay 20 % tariffs to obtain an important percentage of the slabs required to fill our rolling mills. We could not afford to do so.

In short, the TRQ as proposed would be highly harmful to CSI and its 1,000 employees. Please advise the President not to restrict slab imports with the TRQ proposed by the ITC or with any other form of import restraint.

Sincerely,

C. Lourenço Gonçalves
President & Chief Executive Officer
California Steel Industries, Inc.

Duferco Farrell Corporation

15 Roemer Blvd.
Farrell, PA 16121
(724) 983-6464

January 14, 2002

The Honorable Robert Zoellick
United States Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508

RE: Section 201 Investigation On Steel Imports

Dear Ambassador Zoellick:

I am writing this letter on behalf of the 500 employees of Duferco Farrell Corporation to express our concern over the ITC's recommended TRQ on slabs.

The TRQ proposed by the ITC would be injurious to Duferco Farrell even if demand for foreign slab did not exceed the 7 million ton quota level. A TRQ with an above-quota tariff of 20 percent would bid up the price of slab imports in advance of the TRQ starting to bind. As slab buyers enter the market to secure their slab needs ahead of the proposed quota levels, our suppliers will artificially raise prices in response to this demand. The effect would be to create an unfair playing ground and to pick a winner and loser as we would not be able to pass along the higher cost to our customers.

In addition, Duferco Farrell, which only began operations in 1999, will need substantially more slab next year than we did in 2000. Our foreign slab suppliers, however, will not absorb any of the above-quota duties. They will simply sell their slab in other markets or withdraw from the slab market and focus more on finished products that have higher profit margins. Other domestic mills will not replace the foreign slab. They have never exhibited any interest in supplying slab to the merchant market. They would much rather take their slab downstream to take away market share from us for hot-rolled and cold-rolled.

The proposed TRQ would wipe away the slim margins we have in any market. In this current depressed market, we are already losing money, and the import restrictions proposed by the ITC would drive us deeper in the hole.

Please advise the President not to impose a TRQ or any other import restrictions on slab and to ensure that we continue to receive the slabs we need to remain in business. The Shenango Valley of Pennsylvania, our 500 employees, and our $100 million in investments are depending on it.

Sincerely,

Benedict J. Sciortino

Benedict Sciortino
President

OREGON STEEL MILLS

Joe E. Corvin
President and Chief Executive Officer

January 11, 2002

The Honorable Robert Zoellick
United States Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508

RE: Section 201 Investigation on Steel Imports

Dear Ambassador Zoellick:

The tariff-rate quota ("TRQ") on semi-finished steel slab recommended by the ITC would impose an unfair cost burden on Oregon Steel Mills that would tilt the domestic playing field in favor of our domestic competitors that do not depend on slab imports.

The majority of our slab purchases are to support production at our Napa Pipe mill, which produces large diameter line pipe for the transmission of oil and gas. Most of this business is contractual. Beginning in February 2002, Napa Pipe will begin production on [ ] tons of line pipe for the Kern River Expansion project. This contract was negotiated last spring before the Section 201 investigation even began. It is a fixed price contract with no ability to raise the selling price. We will need to import at least [ ] more tons of slab in 2002 than we imported in 2000 in order to fill this contract. The impact of the proposed TRQ on the slab used to supply this contract would be substantial and would likely erase all profit from the contract.

Our foreign suppliers know that we must import slab to fill the Kern River Project. As we stated in our exclusion request for API slabs, virtually no domestic slab is available that would meet the specifications for this contract . While one integrated producer in the East may be able to make the specifications, it is in direct competition with us for the line pipe business, and the cost of freight to the West Coast is prohibitive.

Our foreign slab suppliers would exploit our vulnerability under the proposed TRQ by forcing us to pay a premium to ensure that we obtain the slabs we need before the

The Honorable Robert Zoellick
January 11, 2002
Page Two

above-quota 20 % tariff kicks in. They know that we cannot afford to take the risk of paying tariffs on above-quota imports. Thus, even if demand does not exceed 7 million tons in year one of the TRQ, the TRQ will drive up our slab costs, erode our expected profits on the Kern River Project, and place us at a competitive disadvantage with mills that do not rely on foreign slab.

Accordingly, we urge you to advise the President not to impose the proposed TRQ or any other import restrictions on slab. We need foreign slab to maintain our business model and the 1,900 jobs that it sustains.

Sincerely,

Joe Corwin

Joe Corvin